FISCAL YEARS 2000-2001
PERFORMANCE REPORT

In 1998, to address longstanding deficiencies in the Department's administration of the Federal student aid programs, Congress amended the Higher Education Act of 1965 (HEA) to create a performance-based organization (PBO) for the delivery of Federal student financial assistance.

The legislation established a discrete management unit within the Department to manage operational functions, (i.e., the administration of the information and financial systems[1]) of the programs. These operational functions encompass the administrative, accounting, and financial management functions of the Federal student aid delivery system, including the:

- Collection, processing, and transmission of student aid applicant data;
- Design and technical specifications for software development and systems supporting the delivery of Federal student aid;
- Acquisition of software and hardware and information technology contracts related to the delivery and management of Federal student aid;
- Contracting for the information and financial systems and other support functions, as well as all aspects of contract management; and
- Provision of all customer service, training, and user support activities related to the systems.

In exercising these operational functions, the PBO is subject to the direction of the Secretary. The Office of Postsecondary Education (OPE) is responsible for development of policy and regulations relating to the Federal student aid programs. In March 2002, the PBO, which had been known as Student Financial Assistance (SFA), was renamed Federal Student Aid (FSA).

[1] See section 141(b)(2) of the Higher Education Act of 1965, as amended (20 U.S.C. 1018).

PERFORMANCE GOALS

In the HEA, Congress set out four concrete goals for the PBO to address in its performance plans:

- Improving service to students and other participants in the student financial aid programs, including making the programs more understandable to students and their parents;
- Reducing the costs of administering the programs;
- Improving and integrating the information delivery systems that support the programs; and
- Developing an open, common and integrated delivery system and information system for the programs.

The statute also authorizes the Secretary to identify additional areas to be addressed. In 2001, when Secretary Rod Paige took leadership of the Department, he made it clear that he wanted two things: (1) a clean financial statement audit and (2) the removal of the student aid programs from the General Accounting Office's (GAO) High-Risk List. No goal, the Secretary said, should take precedence over assuring the American people that their tax money was being well managed and wisely administered.

After reviewing the issues related to removing FSA from GAO's High Risk List, the Secretary added improving program integrity to the PBO's goals. Meanwhile, FSA recognized that to accomplish all the goals, the PBO needed to have an effective, well trained, engaged workforce.

IMPROVING CUSTOMER SERVICE

A clear mandate in the HEA was to improve the service students were getting from the Federal Student Aid office. Encouraging the Department's customers to do their business with us online is mandated by the Government Paperwork Elimination Act (GPEA), is a goal in the *Strategic Plan* and the *Blueprint for Management Excellence*, and has been a central thrust of the PBO.

FAFSA ON THE WEB

Our key product and point of service for students is the student aid form—the Free Application for Federal Student Aid (FAFSA). The paper version is one of the biggest print jobs in the Federal government. However, we have tried to encourage applicants to file online—it not only costs less to process an electronic application than a paper one, but we have found that there are fewer errors on electronic applications. The primary reason for this is that there are built-in edit checks that prevent some inadvertent entry errors and reduce others. We can process electronic applications faster, reduce the number of corrections to be made, and deliver a calculation of the expected family contribution (EFC) more quickly, which is helpful to students. We released our first online version of the FAFSA[2] in 1997 and each year since then, we have made it more robust and easier for customers to use. We added a Spanish language option in January of 2001. While the Internet version of the FAFSA has been successful, we understand the need to continue to make paper applications available to students who do not have electronic access. We will continue to work internally and with our partners in the academic community to address this issue.

FAFSA PROCESSING

	1999-2000	**2000-2001**	**2001-2002**
	(Complete[3])	(Complete)	(Complete)
Total FAFSAs	10,209,642	10,544,971	11,399,938
Paper	6,968,489	6,298,288	5,723,570
Web	1,189,256	2,174,025	3,607,388
Other electronic[4]	2,051,897	2,072,658	2,068,980

FORM 2000

Along with e-business, another Departmental goal is reducing our partners' data reporting burden. Dealing with our 3,967 financial partners, we must maintain a balance between accountability and burdensome reporting. We made considerable progress in fiscal year (FY) 2000 when FSA implemented an electronic payment and reporting system for guaranty agencies. "Form 2000" replaced three large paper reports required of guaranty agencies—Forms 1189, 1130, and 704. This Web-enabled data exchange system eases guaranty agencies' reporting burden and it increases their access to data. It also provides increased financial oversight of collection activities, reimbursement claims, and portfolio status.

WEB PORTALS

In March 2000, we launched the first of our Web portals for customers. The Schools Portal[5] presents through a single user-interface all of the disparate resources, many of which are databases, that financial aid advisor*s* need access to in order to do their job. It features "IFAP," our Information for Financial Aid Professionals Web site, where we post all Dear Colleague letters, technical guidance, and news updates, as well as an interactive calendar for Department and community events and deadlines.

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[2] The Internet address for the FAFSA is http://fafsa.ed.gov.
[3] A processing cycle (or "award year") begins January 1 and continues for 86 weeks.
[4] Non-Internet electronic filings include ED Express and FAFSA Express—software applications developed for schools to submit students' FAFSAs electronically. Using the Web version of FAFSA, students can submit their applications directly to FSA over the Internet.
[5] The Internet address for the Schools Portal is http://fsa4schools.ed.gov.

During FYs 2000 and 2001, we also did a lot of development work on Web portals for use by students, lenders, guaranty agencies, and other customers and partners. The Financial Partners Portal, designed with help from the lending community to provide one-stop service, was released in April 2002. The Students Portal followed in May 2002. Both portals simplify access to necessary and useful information for their respective constituencies.

ELECTRONIC SIGNATURES

In July 2001 we launched "e-sign," the first electronic signature option for a Master Promissory Note. We developed authentication standards for e-signatures in the William D. Ford Federal Direct Loan Program. We also made sure these authentication standards were consistent with industry standards used by guarantors and FFEL lenders (those participating in the Federal Family Education Loan Program). Instead of an applicant completing the FAFSA, entrance counseling, and other parts of the student aid process online, then printing the signature page of the promissory note, signing a "wet signature," and mailing the page to the Education Department or their private lender, e-sign enabled the process to be seamlessly electronic from end to end.

e-SERVICING

In FY 2001, we began work on electronic billing and payment in the Direct Loan program. The option for borrowers in repayment to receive and pay their monthly bills online was piloted in January of 2002 and went into full production in March of 2002.

MEASURING IMPROVEMENT IN CUSTOMER SERVICE

In 2000, we sought to measure our improvement in customer service using the American Customer Satisfaction Index[6] (ACSI). For FY 2000, FSA rated 72.9 overall on its core business processes, which was better than the government average (68.6) and the average for banks (68.0), but not as good as the average for private sector financial services (73.9). In FY 2001, we improved our customer satisfaction rating to 74.2, compared with the government average (68.6) and the private sector rating (74.4). While we remain committed to measuring customer satisfaction, we are looking at more relevant surveys for measuring our improvement in customer service.

REDUCING COSTS

Another clear statutory mandate is to reduce the costs of administering the student aid programs. This is a challenge, as both workload and operating costs are increasing. The demand for student aid is going up as the number of high school graduates grows and

[6] The ACSI is a partnership of the American Society for Quality, the University of Michigan School of Business, and the CFI Group, a for-profit "Customer Asset Management" firm. For more detailed information, visit the ACSI Web site at http://www.theacsi.org.

more adults return to school. The rising cost of higher education is also causing more students to apply for financial help. At the other end of the spectrum, as the Direct Loan portfolio matures, more borrowers enter repayment, and servicing costs for loans in repayment are about twice those of loans of borrowers who are still in school.

ACTIVITY-BASED COSTING

To save money, we needed a clear understanding of what we were paying for various facets of our work. Our starting point was to determine how much we paid for each business function or process, so we implemented, and are continuing to fine-tune, an Activity Based Costing (ABC) management information tool.

ABC focuses on the individual activities our office performs. Under ABC, all costs—personnel, contracts, supplies, and so on—associated with each activity are tracked. This cost management tool allows us to determine the cost of processing a FAFSA, originating a Direct Loan, consolidating a loan, collecting a defaulted loan, or reviewing an application for institutional eligibility, for example. In essence, it will allow us to identify and calculate our "unit cost" per business function or process.

This tool allows us to capture not only FSA's cost of personnel, supplies, contracts, and so forth, but also its portion of common, Department-wide services, such as postage, training courses, accounting, and legal services.

UNIT COST

Unit cost can be measured from a number of perspectives. FSA's current attempt at identifying unit cost is to state the overall unit cost as the reach of the budget dollars received for the fiscal year to the unduplicated financial aid recipients for the year. In other words, taking total current fiscal year budget obligations and dividing them by the total number of people served in the fiscal year—grant recipients, new borrowers, and borrowers in repayment. The overall unit cost can also be broken down by individual business process, using this budget costing methodology.

Unit cost calculations indicate that between FY 2000 and FY 2001, our workload, measured by the number of people we served, grew by six percent. Modernized systems, legacy system retirements, and other cost cutting measures kept the increase in total obligations to about three percent—including the costs of additional modernization investments, which totaled $72 million. Our unit cost, calculated by dividing our direct obligations by the number of unduplicated aid recipients, dropped from $20.14 in 2000 to $19.57 in 2001—about 3 percent.

Analysis of this information showed us that some of our costs decreased, but others rose, some because of increased workloads, such as costs for debt collection support, loan consolidation operations and charges for common services. We are currently in the process of fine-tuning our ABC model by refining our definitions and calculations to provide for a better infrastructure in which to report on actual costs each year. This will provide for more targeted actual unit cost information, in support of our effort to control costs and run our operation as efficiently as possible.

PERFORMANCE-BASED CONTRACTS

The statute directed the PBO to maximize the use of performance-based servicing contracts. Since 1998, every new contract has had performance benchmarks built in, and we have gone back to all existing major contracts and transformed them into performance-based contracts. In 2001, we renegotiated the consolidation contract and expect it to result in a reduction in our loan consolidation "unit cost."

The performance transformation initiative also has been welcomed by our operating partners. Our previous approach prescribed how an operating partner must do a job, sometimes specifying great detail that had little or no effect on performance. The new approach holds our operating partners accountable for outcomes rather than inputs.

INTEGRATING SYSTEMS

Another legislative mandate was to integrate our aging computer systems. The systems were expensive to run and hard for students, schools, financial partners, and our staff to use.

We initially laid out plans for integrating and modernizing the student financial aid information and delivery systems in our *Modernization Blueprint*. We developed an enterprise-wide systems architecture to guide development and action. We concluded that the best way to integrate the remaining databases was to employ "middleware," which is an industry-accepted means of tapping into data from multiple databases so as to deliver a "seamless" transaction for the customer.

We are reengineering, retiring, and replacing our old computer systems to achieve integration. In 1998, we started with 14 "stovepipe" computer systems. In November of 2000, we retired the first of the legacy computer systems—the Central Data System (CDS). In 2001, we replaced the proprietary Title IV Wide Area Network (TIV WAN) with an Internet gateway and also replaced the old Campus Based System (CBS). By the end of 2002, we will retire the Financial Aid Recipients System (FARS) and the Financial Partners pieces of the FFEL system and transfer key capabilities to the new FSA Financial Management System.

We will have replaced or reengineered nine of our legacy systems by the end of FY 2002 with the remaining five to be addressed over the next two to three years. As of this reporting, all of the systems integration projects are funded and underway.

As we move forward, we are looking at integrating the data that lies behind our systems and processes to achieve even greater integrity and efficiency. This means consolidating redundant databases and providing a full and true accounting of our systems of record. We need to ensure that we have a single, accurate data source from which to provide customers and others with current and reliable information.

COMMON ORIGINATION AND DISBURSEMENT

Our Common Origination and Disbursement initiative is an example of how systems integration can improve service and program integrity.

In FY 2000, our modernization efforts led us to recognize a lot of commonality in the data collected in the Pell Grant, Direct Loan, and Campus-Based programs and we began development of a single origination and disbursement process for the three programs. The initial release of the Common Origination and Disbursement System was implemented in April 2002. It has one common process, one common record, one common database, one common Web site—that allows close to real-time processing and online updates—and one common service center.

COD uses middleware technology to interact with nine other FSA systems and exchange information with our partners. It allows for the retirement of the old Recipient Financial Management System (RFMS) (Pell Grant) and the DLOS (Direct Loan Origination System) by the end of 2003. Those systems' key functionalities were consolidated into the new COD system along with the addition of new functionality.

A MEASUREMENT OF ACHIEVEMENT: TECHNOLOGY AWARDS

We are pleased at the recognition the Department has received for many of our efforts and products. During 2000 and 2001, we received a number of technology awards:

- 2001 – Government Technology Leadership Award – *e-Sign*
- 2001 – e-Gov Explorer Award, 2000 e Gov Pioneer Award – *FAFSA on the Web*
- 2001 – Digital Government Award, 2000 Government Technology Leadership Award – *Direct Loan Servicing Web Site*
- 2001 – e-Gov Pioneer Award – *Form 2000*
- 2001 – OPM Director's Award of Excellence – *Studentjobs.gov*
- 2000 – e-Gov Trailblazer Award – *Students.gov*

PROGRAM INTEGRITY

We have added program integrity to the list of performance goals. It is a priority for the Administration, which singled out student aid programs in the *President's Management Agenda*. Under Secretary Paige, the Department has placed priority on the elimination of waste, fraud, and abuse, following some highly publicized and embarrassing mistakes and even criminal activity. The Secretary has initiated a Culture of Accountability throughout the Department—he holds his top officers and their staffs accountable for results. In 2001 the Department developed a *Blueprint for Management Excellence* and a new *Strategic Plan*, both of which have specific action items for FSA.

The *Strategic Plan* seeks to develop and maintain financial integrity and management and internal controls throughout the Department. One of the key projects in the *Plan*, and also in the *Blueprint*, is the deployment of Oracle Federal Financials, a software package that will update and integrate FSA and the Department's financial accounting systems. FSA's performance plans have been integrated with these plans.

FINANCIAL MANAGEMENT

In FY 2000, FSA deployed the first of four Oracle Federal Financials modules to begin constructing the Financial Management System (FMS). In FY 2001, we completed the second and third modules to prepare for full deployment in 2002.

Successfully integrating FSA's FMS with the Department's new Oracle Federal Financials accounting system will allow for timely, efficient, and effective reconciliation processes and procedures to be developed and supported among the transactional accounting feeder systems, FSA, the Department, and the U.S. Treasury.

We are now focusing on the quality of the accounting treatment built into the FMS. These are major steps toward earning an unqualified opinion on the annual financial statements.

Although we have not yet reached our goal of receiving a clean audit—unqualified opinions on all five of our financial statements—we have made progress. In 1999, we received an overall qualified opinion on our financial statements. That year, we were cited for four material weaknesses in the *Report on Internal Control*, and we received one disclaimer. In FY 2000, we again received a qualified audit opinion on the financial statements and were cited for three material weaknesses. In FY 2001, we received another qualified audit opinion, but there was only one material weakness—the lack of an integrated financial management system that allows us to accumulate, analyze, and present timely, reliable financial information.

The Department and FSA are committed to earning a clean audit opinion on our FY 2002 financial statements. The implementation of the new financial management systems in FSA and the Department, and the integration of those systems, as well as a concerted focus on improved procedures to support reconciliation processes and analysis, will help deliver that clean audit.

PROGRAM OVERSIGHT

The *Strategic Plan* identifies as an action item getting Federal student aid programs off GAO's High Risk list. A key objective here is improving schools' compliance with the statutory and regulatory requirements for the administration of Title IV Federal student aid. Our goal is to enhance the integrity of the student loan, grant, and work-study programs and continually work toward improvement.

FSA's strategy is to balance enforcement and technical assistance. For a new school to become eligible, it must first meet all statutory and regulatory requirements, then complete pre-certification training. The Department provides ongoing training to participating schools.

Also for continuing schools, our case teams utilize an Institutional Assessment Model to monitor school performance and determine the probability that Federal funds are at risk. This model was reengineered from a "penalty point" model that was based on the school's previous performance to a "probability" model that highlights areas for possible future performance review. The model gives priority to preventing risks, not just controlling them.

The data systems—the National Student Loan Data System, Postsecondary Education Participants System, Campus-Based System, and the new Common Origination and Disbursement—provide the data we need to assess potential risk and conduct effective oversight activities.

The Institutional Assessment Model allows the case teams to analyze schools' prior year trends in funding volumes, default rates, liability assessments, administrative actions, and other data. The outcome is a ranking of the school based on potential risk to student aid funds. This model increases our staff's efficiency and effectiveness. The case teams can continually monitor schools and identify those that appear to warrant more indepth review. The method helps the teams perform more efficiently, helping them prioritize their oversight efforts so as to make the most of limited resources.

Based on initial analyses, the case team makes a decision about whether to conduct an on-site program review at the school to determine whether problems exist. If the on-site program review identifies deficiencies, we require the school to take corrective action, which may include accepting technical assistance we provide, correcting the problem, and paying liabilities we assess. In FY 2001, our assessments resulted in nearly $58 million in recovered liabilities.

For more egregious irregularities, we take other enforcement actions, such as placing the school under "Heightened Cash Monitoring" or on the reimbursement system of payment (as opposed to the cash advance system), fining or terminating the school, and debarring the school and its owners or principals. If a school's past performance indicates its financial viability is at risk, we require a letter of credit. We currently are holding almost $100 million in letters of credit to protect student aid funds. We also partner with accrediting agencies and state entities in joint compliance efforts.

In FY 2001, we monitored the compliance components that give us the overall picture of each school's compliance, (e.g., compliance audits, audited financial statements, default rates, and risk assessment rank). Our Institutional Assessment Model moved us to provide more indepth management for 40% of participating schools. That means one or more risk factors presented themselves to warrant closer scrutiny. So we did a thorough, comprehensive compliance review, using all the tools at our disposal, for two out of every five of the 6,160 schools participating in Title IV. The majority of schools were found to be administering the programs appropriately.[7]

FY 2000 OVERSIGHT ACTIVITIES

Case Management & Oversight teams:

- Recertified 1,800 schools
- Conducted 5,500 compliance audits and resolved 1,200 with significant deficiencies
- Performed 6,200 financial statement reviews and resolved 850 with deficiencies
- Conducted 136 on-site program reviews
- Put 74 schools on reimbursement payment status
- Initiated 34 administrative actions

FY 2001 OVERSIGHT ACTIVITIES

- 2,450 school recertifications
- 5,700 reviews of compliance audits and resolved 1,640 with significant deficiencies
- 5,500 financial statement reviews and resolved 1,436 with deficiencies
- 172 on-site program reviews
- 72 schools placed on reimbursement payment status
- 20 administrative actions initiated

The new Common Origination and Disbursement system, in addition to providing an integrated origination and disbursement solution will make a major contribution to strengthening program integrity. It will allow us to look at reporting and funding from different perspectives. We will be able to compare schools' origination and disbursement activity in a variety of ways—by type of institution, geographical location, time period, etc. This will enable us to look at patterns and more closely guard Federal funds. If a school fails to account for its drawdowns, the case management team will get a non-compliance flag and be able to shut off the flow of funds when appropriate.

FOREIGN SCHOOL OVERSIGHT

Foreign institutions present unique compliance challenges. Factors such as national policies, the lack of a Financial Aid Office (some countries do not provide student aid

[7] It should be noted that the Higher Education Amendments of 1992 provided the Department with tools to terminate the eligibility of schools with high default rates. As a result, by the late 1990s, approximately 1,000 poor-performing schools was removed from participation in Title IV student aid programs.

and others administer it differently from the United States), distance from the United States, different academic requirements, varied currencies and accounting standards, and language complicate communication and enforcement of the HEA and regulations.

FSA provided special training to foreign schools to ensure they certify loan applications and make sure the American students are accepted to the school before funds are disbursed. We also communicated to FFEL lenders their responsibility to notify the school once a loan is disbursed. These requirements do not prevent fraud but they do give the school and the Department early notice that loan funds have been provided to a student who may not be enrolled, as anticipated. During 2001, we also started work on a student aid handbook designed especially for foreign schools. The *Foreign School Handbook* was distributed in May of 2002.

FOREIGN SCHOOLS FY 2000-2001

- 507 schools
- 13,400 American students
- $225 million in Federal student aid
- 66.5% of schools received less than $100,000 annually
- 51 large schools received more than $500,000 annually (85% of volume)
- Avg. default rate 2.2%

PARTNERS IN OVERSIGHT

In addition to our oversight of schools, FSA conducts reviews of guaranty agencies (GAs) and lenders. GAs also conduct reviews of lenders and schools. We work with our financial partners to address issues that affect program integrity, such as default management.

DEFAULT MANAGEMENT

During FY 2000, the Cohort Default Rate, which measured defaults from the cohort of borrowers that went into repayment in FY 1998, dropped to 6.9%. The FY 2001 Cohort Default Rate, reflecting the FY 1999 cohort, fell to an historic low of 5.6%.

While economic conditions affected the default rates, so did a community-wide effort by schools and lenders to reduce defaults. Also, the Higher Education Amendments of 1992 gave the Department additional tools that were needed to terminate the eligibility of high default schools. The result was a 75% reduction from the FY 1990 rate of 22.4%.

The Department's partnership efforts with Historically Black Colleges and Universities (HBCUs) have helped these schools manage their default rates to a point that for FY 1999 (released in FY 2001) none of the schools were subject to sanctions. Our strategies with HBCUs have included schools' development of acceptable default management plans and engagement of independent third parties to help with implementation. We follow up with technical assistance as needed. We also focus special default prevention assistance for Hispanic Serving Institutions and Tribally Controlled Colleges.

In October of 2000, the Department convened and hosted a community-wide Student Loan Repayment Symposium. Every sector of the industry—schools, lenders, guaranty agencies, students—was represented. The three-day meeting resulted in the publication of a guidebook of best practices for all student aid practitioners, as well as a new focus on default prevention and aversion throughout the lifecycle of a loan.

In August of 2001, FSA held its first National Default Prevention Day, coordinating and conducting simultaneous default management and prevention trainings at locations nationwide. We targeted schools with unacceptably high default rates. More than 750 schools voluntarily participated.

DEBT COLLECTION

Another measure of program integrity is the collection and recovery of defaulted student loans. In FY 1998, before FSA was established as a PBO, the Department implemented performance-based debt collection contracts with private sector collection agencies. As a result, collections on defaulted student loans through agencies increased from $96 million in FY 1998 to $191 million in FY 1999, $228 million in FY 2000, and $230 million in FY 2001.

During this period collections on defaulted loans from all sources, including guaranty agency collections and Treasury offsets, increased from $1.94 billion in FY 1999 to $2.77 billion in FY 2000 and $2.44 billion in FY 2001.

The PBO also stepped up consolidation efforts to resolve defaulted student loans. In FY 1998, consolidations of defaulted loans, FFEL and Direct combined, totaled $821 million. Consolidations of defaulted loans increased to $1.82 billion in FY 2000 and $2.68 billion in FY 2001.

In September of 2000, the Department signed an agreement that resulted in even greater progress in recouping defaulted loans. Under an agreement with the U.S. Department of Health and Human Services, FSA began matching defaulted debtor records against their National Directory of New Hires (NDNH) database. In December 2000, FSA conducted its first data match, and during FY 2001 it located 500,000 defaulted borrowers who previously were identified as "non-locatable." The data matches that year alone resulted in the collection of $133 million in defaulted loans.

In May 2001, the Department of Education was the only Federal agency granted a permanent waiver from the debt transfer and cross-servicing requirements of the Department of the Treasury under the Debt Collection Improvement Act because of the Department's effectiveness in collections.

ERRONEOUS PAYMENTS

GAO has reported that our inability to verify students' income is a weakness that makes our programs vulnerable to fraud and error. The FY 2002 *President's Management Agenda* cited estimates of Federal Pell Grant Program over-awards at up to $400 million and under-awards at more than $100 million.

In FY 2001, the Department worked with the Internal Revenue Service (IRS) on a statistical test match to verify income. The final results of our work with the IRS determined over-awards for the 2000-2001 school year totaled close to $272 million and under-awards about $64 million, far less than earlier estimates, but still significant errors. (See "Legislative Recommendations" on page 14.)

OTHER MAJOR ACCOMPLISHMENTS

EMPLOYEE ENGAGEMENT

We recognized from the outset that if the PBO were to be effective in integrating systems, reducing costs, and improving customer service that the employees needed to have the proper skills, knowledge, tools, guidance, and leadership to do their jobs. We found that although many staff members might have done their individual jobs well, they did not have a sense of what their role was, how they fit into the overall delivery of student aid, or who their primary customer was. Further, in an FY 1999 government survey, FSA's employee satisfaction ranked near the bottom: 38th out of 49 Federal agencies.

To improve FSA's effectiveness, we restructured the organization into three customer channels designed to serve students, schools, and financial partners. By this restructuring, and by providing training to all staff on the various student aid programs, the application process, and the performance and accountability philosophy of the PBO, we provided a context for each job.

We used the Gallup Organization's 12 question Gallup Workplace Management survey, known as the "Q12," to measure employee engagement. Follow-up surveys recorded improvement in employee satisfaction, but we have determined that it is more important to emphasize enhanced performance—providing the necessary tools and training—than to measure satisfaction, per se.

VFAs

The Higher Education Act Amendments of 1998 authorized the Secretary to enter into Voluntary Flexible Agreements (VFAs) with guaranty agencies, replacing the standard agency agreements. In 2000-2001, the Department signed agreements with four agencies—American Student Assistance, California Student Aid Commission, Great

Lakes Higher Education Guaranty Corporation, and Texas Guaranteed Student Loan Corporation.

Each of the four VFAs was designed to test different innovations within the FFEL program, but the innovations have a common theme—to improve the efficiency of collections and shift incentives from the back-end (defaulted loan collection) to the front-end (avoiding default altogether). If successful, these approaches will support our goal to strengthen program integrity by enhancing default prevention.

In early 2002, the Department delivered an *Interim Report to Congress: Impact of Voluntary Flexible Agreements in the Federal Family Education Loan Program* and also established common, general measures for evaluating each VFA's performance. The Department will submit an additional report to Congress in early 2003.

LEGISLATIVE RECOMMENDATIONS

The PBO legislation requires the chief operating officer to advise the Secretary on policy matters that affect the operations of Federal student aid programs and, in this report, make recommendations for legislative changes that would improve operations.

FSA makes suggestions and offers advice to the Office of Postsecondary Education (OPE) and the Office of the Deputy Secretary on policy, regulatory, and legislative issues related to the operational aspects of student aid. We work closely with OPE on negotiated rulemaking—helping to formulate and discuss issues, providing data, background analysis, "front line" experience, and input on potential operational impacts of the proposals to be used for consideration during reauthorization of the HEA.

STATUTORY CHANGE NEEDED TO IMPROVE INCOME VERIFICATION

The Department believes routine data matches with the Internal Revenue Service (IRS) would strengthen the financial integrity of the student aid programs. The matches would allow the verification of applicant income information submitted on the student aid form. We recommend the Internal Revenue Code be amended to allow for these data matches and the Administration included a request in the 2003 budget to provide additional authority for this verification. Subsequently, on August 9, 2002, the Secretary of Treasury, Secretary of Education, and Director of the Office of Management and Budget sent proposed legislation to Congress.

CONCLUSION

FSA has made significant progress in improving customer service and has taken several important steps toward better systems integration. We have formed a number of partnerships within the student aid community to improve service to students and their families. Our customers are responding positively to the changes we are making in our systems and products. We have retired and replaced some outdated systems, improved system integration, and will continue to review our legacy systems for reengineering, retirement, and replacement.

While there has been progress in reducing unit costs in some areas, such as the greater use of electronic application filing, costs in other areas have increased, and overall costs are higher than they should be. Many other challenges still remain. The lessons that we have learned in the last two years and the recent efforts of Secretary Paige to improve management and accountability in the Department provide us with knowledge and top-level commitment necessary to achieve our goals and priorities and to deliver results.